

Message Text

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ACTION ARA-06

INFO OCT-01 SS-14 ISO-00 L-01 EB-03 TRSE-00 CIEP-01 COME-00

INR-05 NSC-05 NSCE-00 CIAE-00 SP-01 EA-06 INRE-00

SSO-00 /043 W

----- 111234

O 122140Z NOV 75

FM AMEMBASSY LIMA

TO SECSTATE WASHDC IMMEDIATE 7598

C O N F I D E N T I A L LIMA 9371

LIMDIS

FOR ARA - WILLIAM ROGERS; L - MARK FELDMAN; EB - THOMAS ENDERS;
TREASURY - JOHN BUSHNELL; CIEP - WAYNE SHARPE; COMMERCE -
DAN ARRILL

EO 11652: GDS

TAGS: EIND, EINV, EMIN, PFOR, PE

SUBJECT: MARCONA EXPROPRIATION - MORNING MEETING WITH GOP
TECHNICAL TEAM, NOVEMBER 11

REFS: A) LIMA 9310, B) LIMA 9304, C) LIMA 9303

1. SUMMARY: MEMBERS OF U.S. GROUP, HEADED BY FISHLOW, MET
FOR TWO HOURS WITH SELECTED MEMBERS GOP COMMISSION (LED BY
BROUSSET, WITH REPRESENTATION FROM TECHNICAL LEVEL OF
MINISTRY OF MINES, COFIDE, FINANCE MINISTRY) MORNING OF
NOVEMBER 11. GOP SIDE'S ESSENTIAL AIM WAS TO COUNTERACT
STRONG U.S. POSITION ON VALUATION TAKEN YESTERDAY AS REPORTED
REF. C GOP CALLED INTO QUESTION ASSUMPTIONS UNDERLYING USG
APPROACH TO ONGOING CONCERN VALUE AND INTRODUCED NEW ELEMENTS
OF CONCERN TO GOP SIDE IN REACHING BOTTOM-LINE FIGURE
BASED ON NET BOOK VALUE. THESE ELEMENTS INCLUDED CITING
OF OUTSTANDING TAX CLAIMS BASED ON "ILLEGAL" SALES COM-
MISSIONS, ALLEGED "HIGH-GRADING" OF MINE BY CHANGING
ANGLE OF MINE PIT SLOPES AND SUGGESTION THAT MARCONA OBTAIN
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NEW AUDIT OF ITS BOOKS FROM PRICE WATERHOUSE AS OF THE

DATE OF EXPROPRIATION. BROUSSET MADE POINT THAT PRIOR TO WORKING OUT DETAILS OF ANY FINAL AGREEMENT, HIS GROUP REMAINS KEENLY INTERESTED IN WORKING OUT AN ORE SHIPPING AND SALES AGREEMENT TO GET ORE MOVING. AT FULL WORKING SESSION OF BOTH TEAMS SCHEDULED FOR AFTERNOON, GOP PROMISED TO PRESENT ITS CURRENT THINKING ON NET BOOK VALUE OF MARCONA ASSETS AND ITS RATIONALE BEHIND THESE FIGURES. END SUMMARY.

2. PERUVIANS BEGAN DISCUSSION BY REQUESTING THAT U.S. TEAM EXPLAIN THE \$20 MILLION DISCREPANCY IN NET BOOK VALUE FIGURES BETWEEN MARCONA'S U.S. AND PERUVIAN ACCOUNTS. FISHLOW POINTED OUT THAT THE MAJOR DIFFERENCE REFLECTS ALTERNATIVE TAX RATES AND DEPRECIATION METHODS BETWEEN PERU AND THE U.S. HE WENT ON TO EXPLAIN THAT THE PERUVIAN CALCULATIONS INTRODUCE A DOWNWARD BIAS IN ASSET VALUATION BECAUSE MUCH OF MARCONA'S EQUIPMENT WAS PURCHASED IN DOLLARS AND WAS VALUED IN LOCAL CURRENCY TERMS AT ARTIFICIAL AND RELATIVELY UNFAVORABLE EXCHANGE RATES. U.S. TEAM STRESSED THE ADVANTAGES OF A GOING CONCERN VALUATION PROCEDURE WHICH TAKES INTO ACCOUNT FUTURE EARNINGS POTENTIAL.

3. PERUVIANS THEN BROUGHT UP FACT THAT IN CONSIDERING MARCONA CASE ONE MUST FULLY TAKE INTO ACCOUNT THE LIABILITIES OF MARCONA. CRITICISM OF MARCONA CENTERED ON FOLLOWING POINTS:

A) FRENCH COMPANY WHICH EXAMINED SAN NICOLAS FACILITIES FOUND THAT MARCONA "HIGH-GRADED" THE MINE, THAT ITS MINEABLE ANGLE OF PITS WAS TOO STEEP AND NOT DESIGNED TO EXTRACT ORE AT PROPER RATE FOR COMPLETE EXPLOITATION OF MINE'S TOTAL RESERVES. (FISHLOW NOTED THAT MARCONA MAINTAINS THAT THEIR PIT ANGLES WERE TECHNICALLY CORRECT.)

B) GOING CONCERN PROJECTION SHOULD NOT BE BASED ON ASSUMPTION THAT MARCONA WOULD CONTINUE TO OPERATE THROUGH 1984 SINCE CONTRACTS EXPIRE IN 1982. U.S. TEAM POINTED OUT THAT MARCONA PROJECTIONS ASSUMED ORE FROM THE LA JUSTA MINE WOULD BE AVAILABLE TO FEED THE PROCESSING FACILITIES

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IN SAN NICOLAS IN THIS INTERIM PERIOD. GOP TECHNICAL EXPERTS POINTED OUT INCREASED COSTS OF PRODUCTION ASSOCIATED WITH THIS ASSUMPTION WHILE U.S. TEAM STRESSED NEED TO ALSO TAKE INTO ACCOUNT SALVAGE VALUE OF SAN NICOLAS PROCESSING FACILITY WHICH ACCORDING TO MARCONA'S CONTRACTS DOES NOT REVERT BACK TO PERU.

C) PERUVIANS THEN INTRODUCED TAX CLAIM WHICH HERE-

TOFORE HAS NOT BEEN ADDRESSED DIRECTLY BY GOP SIDE. ESSENTIALLY IT RELATED TO FACT THAT PERUVIAN LAW DOES NOT PROVIDE FOR MORE THAN TWO PERCENT WHILE MARCONA'S CONTRACTS PROVIDED FOR FOUR PERCENT WHILE MARCONA'S CONTRACTS PROVIDED FOR FOUR PERCENT COMMISSION ON THE CIF VALUE. THUS, PERUVIANS SAID MARCONA SHOULD HAVE WITHHELD TAXES FROM ITS SAN JUAN OPERATION OF ABOUT \$6 MILLION AND THAT TOTAL TAX LIABILITY MIGHT BE IN RANGE OF \$30 MILLION. A TAX CLAIM ON THOSE GROUNDS HAD BEEN PRESENTED TO MARCONA IN FEBRUARY 1975, BUT HAD BEEN IGNORED BY MARCONA. BROUSSET SUGGESTED THAT MARCONA'S LEGAL REPRESENTATIVES SHOULD NOW APPROACH GOP TAX AUTHORITIES TO SEE IF A SATISFACTORY SOLUTION TO THIS CLAIM COULD BE WORKED OUT, AS ANY OVERALL COMPENSATION SETTLEMENT WOULD REQUIRE ALL LOOSE ENDS TO BE TIED UP. BROUSSET ADDED THAT MARCONA HAD PREVIOUSLY STATED THAT IT NEEDED ACCESS TO HIERROPERU BOOKS TO OBTAIN NECESSARY DATA AND THAT MARCONA COULD NOW GO TO HIERROPERU FOR REQUIRED INFORMATION. BROUSSET ALSO SUGGESTED IT WOULD BE USEFUL FOR MARCONA TO OBTAIN AN END AUDIT OF ITS BOOKS AS OF DATE OF EXPROPRIATION. GOP WOULD HAVE NO OBJECTION IF PRICE WATERHOUSE UNDERTOOK SUCH AN AUDIT.

4. BEFORE CLOSING MEETING, BROUSSET MADE PITCH FOR BOTH SIDES TO FIND WAY TO GET ORE MOVING IN WORLD MARKETS, APART FROM DETAILS OF ANY FINAL SETTLEMENT. HE SAID THAT AT THE AFTERNOON MEETING GOP TEAM WOULD PRESENT ITS CALCULATIONS OF ADJUSTED BOOK VALUE USING PERUVIAN METHODOLOGY USED IN PRIOR PERUVIAN EXPROPRIATION CASES. HE THEN REITERATED NEED TO FIND A MUTUALLY ACCEPTABLE SETTLEMENT WHICH PERUVIANS COULD JUSTIFY IN DOMESTIC POLITICAL TERMS.

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5. COMMENT: GOP TEAM'S PRESENTATION WAS TACTICALLY PREDICTABLE IN TERMS OF CALLING INTO QUESTION SOME OF OUR ASSUMPTIONS PRESENTED MONDAY AND, IN EFFECT, GAVE US A DOSE OF OUR OWN MEDICINE. IF ONE ACCEPTS THEIR APPROACH TO VALUATION (NET BOOK VALUE), THEN ONE WOULD HAVE TO CONCEDE THE VALIDITY OF SOME OF THEIR BASIC ARGUMENTS. WE DO NOT ACCEPT THIS CONTENTION BUT ARE PREPARED TO EXPLORE ANY FORMULATION WHICH EVENTUALLY WILL PRODUCE A MUTUALLY ACCEPTABLE AMOUNT. ALSO, RAISING TAX ISSUE AT THIS TIME IS PROBABLY BENEFICIAL SINCE IT WILL HAVE TO BE DEALT WITH SOONER OR LATER, AND IT IS PREFERABLE THAT WE CLARIFY THE TAX PROBLEMS NOW RATHER THAN AT THE ELEVENTH HOUR WHERE THEY WOULD BE CERTAIN TO SURFACE IN ANY CASE.
DEAN

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Message Attributes

Automatic Decaptioning: Z
Capture Date: 01 JAN 1994
Channel Indicators: n/a
Current Classification: UNCLASSIFIED
Concepts: NATIONALIZATION, NEGOTIATIONS
Control Number: n/a
Copy: SINGLE
Draft Date: 12 NOV 1975
Decaption Date: 28 MAY 2004
Decaption Note: 25 YEAR REVIEW
Disposition Action: RELEASED
Disposition Approved on Date:
Disposition Authority: GolinoFR
Disposition Case Number: n/a
Disposition Comment: 25 YEAR REVIEW
Disposition Date: 28 MAY 2004
Disposition Event:
Disposition History: n/a
Disposition Reason:
Disposition Remarks:
Document Number: 1975LIMA09371
Document Source: CORE
Document Unique ID: 00
Drafter: n/a
Enclosure: n/a
Executive Order: GS
Errors: N/A
Film Number: D750394-0370
From: LIMA
Handling Restrictions: n/a
Image Path:
ISecure: 1
Legacy Key: link1975/newtext/t19751151/aaaabtdh.tel
Line Count: 169
Locator: TEXT ON-LINE, ON MICROFILM
Office: ACTION ARA
Original Classification: CONFIDENTIAL
Original Handling Restrictions: LIMDIS
Original Previous Classification: n/a
Original Previous Handling Restrictions: n/a
Page Count: 4
Previous Channel Indicators: n/a
Previous Classification: CONFIDENTIAL
Previous Handling Restrictions: LIMDIS
Reference: 75 LIMA 9310, 75 LIMA 9304, 75 LIMA 9303
Review Action: RELEASED, APPROVED
Review Authority: GolinoFR
Review Comment: n/a
Review Content Flags:
Review Date: 11 SEP 2003
Review Event:
Review Exemptions: n/a
Review History: RELEASED <11 SEP 2003 by CunninFX>; APPROVED <17 SEP 2003 by GolinoFR>
Review Markings:

Margaret P. Grafeld
Declassified/Released
US Department of State
EO Systematic Review
06 JUL 2006

Review Media Identifier:
Review Referrals: n/a
Review Release Date: n/a
Review Release Event: n/a
Review Transfer Date:
Review Withdrawn Fields: n/a
Secure: OPEN
Status: NATIVE
Subject: MARCONA EXPROPRIATION - MORNING MEETING WITH GOP TECHNICAL TEAM, NOVEMBER 11
TAGS: EIND, EINV, EMIN, PFOR, PE, US, MARCONA
To: STATE
Type: TE
Markings: Margaret P. Grafeld Declassified/Released US Department of State EO Systematic Review 06 JUL 2006